SEPTEMBER 1985 QUARTERLY REPORT

Surveys of Consumer Attitudes

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Third Quarter Surveys
July-September 1985

October 11, 1985

INTEREST RATE REDUCTIONS PROPEL BUYING ATTITUDES TO NEW PEAKS

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HIGHLIGHTS

- In the third quarter 1985 survey, the Index of Consumer Sentiment was 92.8, just below the 94.3 recorded one quarter earlier, and down from 98.9 one year earlier. The small declined recorded during the past year reflects the expectation that economic growth will remain slow, yielding no further declines in unemployment. Nonetheless, this was the tenth consecutive quarter with an Index figure in the 90s—ranging from 91.5 to 99.5—the longest and highest sustained period of consumer optimism recorded since the 1960s. Moreover, discounts on prices and interest rates have propelled consumer buying attitudes to new all time record levels in the third quarter 1985 survey.

- Among families with incomes of $25,000 or more, the Index stood at 102.4 in the third quarter survey, down from 104.2 in the second quarter, and 107.9 in the third quarter of 1984.

- More families favorably rated buying conditions for homes in the third quarter 1985 survey than at any other time in the history of these surveys. Among all families, 71 percent held favorable home buying attitudes, surpassing the prior record of 65 percent recorded in 1977. The availability of reduced mortgage interest rates was mentioned by 52 percent of all families, the highest level ever recorded. These record home buying attitudes were also supported by the most favorable perceptions of market prices for homes in more than twenty years.

- The third quarter 1985 survey also recorded the most favorable evaluations of buying conditions for new vehicles in more than thirty years. Among all families, 67 percent held favorable car buying attitudes in both the second and third quarter 1985 surveys, substantially above the prior cyclical peak of 51 percent recorded in the second quarter of 1978. Reports about the availability of reduced interest rates on vehicle loans doubled in frequency during the past year, and have been primarily responsible for the resurgence in favorable vehicle buying attitudes.

- Many fewer consumers expected the economy to improve during the year ahead in the third quarter 1985 survey (25 percent) than one year earlier (33 percent), or at the 1983 cyclical peak (52 percent). Although the 25 percent recorded in the third quarter is the lowest level since early 1980, there has only been a small increase in the proportion of families that expected the national economy to actually worsen—15 percent in the third quarter of 1985, just above the 14 percent recorded one year earlier. The shift in consumer opinion has been toward the view that the economy would continue on its current slow pace of expansion—reported by 57 percent in the third quarter, up from 49 percent one year earlier, and the highest level since the 1960s.

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The response of consumers to the recent interest rate reductions has demonstrated not only their willingness to spend, but also their resolve to wait for discounts on prices and interest rates. The maintenance of high sales levels depends on the continuation of these discounts.

Although consumers now believe that the upward momentum in the economy has been drained, few expect actual declines to follow. Good economic news has now lost its ability to stimulate further improvement in sentiment due to habituation—for example, the recent news about the low level of inflation attracted little attention. As a result of habituation to favorable news, consumers have become more sensitive to unfavorable developments. But isolated bits of news lack the ability to sustain widespread and cumulative changes in mass attitudes. Cumulative declines in sentiment require a focal point to integrate diverse economic developments. None has yet emerged—neither of the twin deficits has served this function for consumers. And some of the traditionally important components of a gathering storm are missing, namely, rising concern with inflation and falling confidence in the government's ability to maintain the current expansion.

Home Buying Attitudes
Reach Record Favorable Level

Attitudes toward buying conditions for homes reached a new all time favorable level in the third quarter 1985 survey. Favorable home buying attitudes were held by 71 percent of all families in the third quarter 1985 survey, up from 50 percent one year earlier. This surpasses the prior cyclical high of 64 percent recorded in the second quarters of both 1983 and 1985, and is above the prior peak of 65 percent recorded in the second quarter of 1977.

The resurgence of favorable home buying attitudes during the past year has been due to declines in mortgage interest rates. In the third quarter 1985 survey, 52 percent of all families cited reductions in mortgage rates in support of their favorable views, more than twice the 22 percent recorded one year earlier (see Table A). And complaints about high mortgage interest rates fell to 14 percent in the third quarter of 1985 from 38 percent one year earlier. Unlike the rebound in home buying attitudes in early 1984, which was propelled by more frequent reference to borrowing-in-advance of potential interest rate increases, the current resurgence has not been accompanied by increased concern that the declines would be brief. In the third quarter 1985 survey, just 5 percent of all families cited the advantage of borrowing-in-advance, down from 14 percent one year earlier, and the peak of 20 percent in the second quarter of 1984.

Favorable perceptions of market prices for homes also supported these very positive home buying attitudes. Among all families in the third quarter 1985 survey, 23 percent referred to the availability of good buys on homes, up from 14 percent one year earlier, and replicating the 20 year peak last recorded in early 1983. In comparison, 12 percent of all families in the third quarter of 1985 survey complained about high home prices, the lowest level in more than two decades.

Record Auto Buying Attitudes
Sustained by Interest Rate Reductions

Attitudes toward buying conditions for vehicles reached a new record level in the third quarter 1985 survey. Among all families, 67 percent held favorable car buying attitudes in the third quarter, unchanged from the second quarter 1985 reading. Unfavorable vehicle buying attitudes, however, fell

slightly to 24 from 27 percent, making the third quarter the most favorable balance of opinion ever recorded.

Interest rate reductions offered by vehicle manufactures have been responsible for sustaining buying attitudes at these very favorable levels. Among all families in the third quarter 1985 survey, 38 percent cited reduced interest rates when asked to explain their views, up from 29 percent in the second quarter, and nearly three times the 13 percent recorded one year earlier (see Table A). Price discounts on new vehicles were mentioned by 24 percent of all families in the third quarter, just below the 26 percent in the second quarter and slightly above the 21 percent recorded one year earlier.

Favorable attitudes toward buying conditions for large household durables were held by 72 percent of all families in the third quarter 1985 survey, just below the all-time peak of 74 percent recorded both one and two quarters earlier. Favorable perceptions of market prices for household durables have been primarily responsible for the maintenance of buying attitudes at record levels. Among all families in the third quarter of 1985 survey, 38 percent mentioned the availability of discounted prices, compared with just 12 percent that registered complaints about high prices. Perceptions of market prices for household durable goods have been more favorable during the past two years than at any time since the early 1960s.

Personal Finances Remain Favorable

The personal financial situation of American families remained favorable in the third quarter 1985 survey. An improved financial situation was reported by 42 percent of all families in the third quarter survey, between the 41 percent recorded in the second quarter of 1985 and the cyclical peak of 45 percent recorded one year earlier. Even after this small decline, evaluations of financial progress have remained more favorable than at anytime during the prior 10 years. Twice as many families reported income increases as reported declines in the third quarter 1985 survey (32 versus 15 percent), a somewhat smaller margin than a year ago (36 versus 13 percent). B On balance consumers continue to hold a positive outlook for their financial situation during the year ahead. In the third quarter 1985 survey, 35 percent of all families expected their financial situation to improve, just below the 37 percent recorded one

year earlier, and the cyclical peak of 41 percent recorded at the start of 1984. Just 12 percent of all families in the second quarter 1985 survey expected their financial situation to worsen during the year ahead.

The small decline in financial prospects can be traced to less favorable income expectations. Among all families in the third quarter survey, 56 percent expected income increases, down from 64 percent one year earlier. Income declines were expected by 14 percent of all families in the third quarter, unchanged from the second quarter reading, and above the year earlier figure of 11 percent. Slower growth in nominal incomes was partially offset as consumers expected the annual rate of inflation to average 4.2% in the third quarter, the lowest quarterly reading in more than a decade.

The continuation of favorable personal financial prospects has maintained consumers' willingness to use accumulated savings or to incur new debt in order to make major purchases. Among all families in the third quarter survey, 36 percent reported their willingness to use savings, just below the 40 percent cyclical peak recorded one year earlier (see Table B). Willingness to incur new debt was reported by 29 percent of all families in the third quarter 1985 survey, up from 27 percent one and two years earlier (see Table C).

Slow Growth Limits Job Prospects

During the past two years there has been a sharp decline in the proportion of consumers that expected continued improvement in the national economy. In the third quarter 1985 survey, 25 percent of all families expected the economy to improve, down from 33 percent one year earlier, and the all time peak of 52 percent in the second quarter of 1983. This sharp fall in favorable expectations, however, was not mirrored by a comparably sharp rise in unfavorable expectations. A worsening economy was expected by only 15 percent of all families in the third quarter 1985 survey, just above the 14 percent recorded in 1984. Most of the shift in opinion during the past two years has been towards the expectation that the performance of the national economy would remain unchanged during the year ahead, rising to 57 percent in the third quarter of 1985, from 49 percent in 1984, and 39 percent in 1983.

Because slower growth but no recession is expected, consumers view the economic outlook in somewhat dulled but nonetheless favorable terms. Among all families in the third quarter survey, 55 percent expected good times financially in the economy as a whole during the year ahead, down from 63 percent one year earlier. Although the third quarter 1985 reading is the lowest level recorded during the past two years, it remains as favorable as the late 1970s peak.

The primary concern expressed by consumers about the outlook for continued slow economic growth involves limited job prospects. When consumers were asked about recent economic developments that they had heard and could recall, references to gains in employment fell to 13 percent in the third quarter of 1985, from 20 percent one year earlier, while reports of rising unemployment increased to 22 from 14 percent. The proportion of families that expected the national unemployment rate to decline during the year ahead fell to just 15 percent in the third quarter 1985 survey, from 25 percent one year earlier, and a high of 40 percent in 1983. A rising unemployment rate was expected by 29 percent of all families in the third quarter of 1985, up from 21 percent in 1984 and a low of 15 percent in 1983. That only small change were foreseen is supported by the majority opinion (54 percent) that the unemployment rate would remain largely unchanged during the year ahead.

Summary Outlook

The response of consumers to the recent interest rate reductions has demonstrated not only their willingness to spend, but also their resolve to wait for discounts on prices and interest rates. The maintenance of high sales levels depends on the continuation of these discounts.

Although consumers now believe that the upward momentum in the economy has been drained, few expect actual declines to follow. Good economic news has now lost its ability to stimulate further improvement in sentiment due to habituation—for example, the recent news about the low level of inflation attracted little attention. As a result of habituation to favorable news, consumers have become more sensitive to unfavorable developments. But isolated bits of news lack the ability to sustain widespread and cumulative changes in mass attitudes. Cumulative declines in sentiment require a focal point to integrate diverse economic developments. None has yet emerged—neither of the twin deficits has served this function for consumers. And some of the traditionally important components of a gathering

storm are missing, namely, rising concern with inflation and falling confidence in the government's ability to maintain the current expansion.

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The third quarter 1985 survey included 1945 interviews conducted between July 5 and September 27, 1985.

TABLE A

REFERENCES TO INTEREST RATES IN SUPPORT OF FAVORABLE BUYING CONDITIONS

Survey Date	Durables		Houses		Vehicles	
	Low Rates	BiA Rates	Low Rates	BiA Rates	Low Rates	BiA Rates
Jan-Mar 1980	1	3	2	7	1	2
Apr-Jun 1980	1	2	6	3	2	1
Jul-Sep 1980	3	2	16	9	2	1
Oct-Dec 1980	1	2	3	8	1	2
Jan-Mar 1981	1	1	1	4	2	1
Apr-Jun 1981	*	2	3	4	2	1
Jul-Sep 1981	1	1	3	4	3	1
Oct-Dec 1981	1	1	2	2	4	*
Jan-Mar 1982	1	1	4	3	3	1
Apr-Jun 1982	1	1	4	2	8	1
Jul-Sep 1982	2	1	7	3	6	1
Oct-Dec 1982	5	1	25	5	18	1
Jan-Mar 1983	7	1	35	5	31	1
Apr-Jun 1983	12	2	48	9	38	2
Jul-Sep 1983	11	2	36	11	30	3
Oct-Dec 1983	6	1	29	10	18	2
Jan-Mar 1984	8	2	36	11	19	3
Apr-Jun 1984	7	5	25	20	14	6
Jul-Sep 1984	6	3	22	14	13	6
Oct-Dec 1984	8	3	30	9	12	3
Jan-Mar 1985	9	2	41	8	22	2
Apr-Jun 1985	10	2	40	9	26	3
Jul-Sep 1985	14	1	52	5	38	1

NOTE: The proportions given above provide greater detail than is reported in the quarterly tables (see Tables 27, 29, and 31). The quarterly tables report the total proportion of respondents that made favorable references to credit conditions. The figures above divide this total into those respondents that referred to the current availability of low interest rates, and those that referred to borrowing-in-advance of rising interest rates.

TABLE B

OPINIONS ABOUT WHETHER NOW IS A GOOD TIME TO USE SAVINGS FOR MAJOR PURCHASES

(Percentage distribution of families with savings)

	Use of Savings...						
Survey Date	OK; not reluctant	Pro-con	Not OK; reluctant	Don't know; NA	Total	# cases	Relative score
Jul-Sep 1980	30%	1%	60%	9%	100%	616	70
Jul-Sep 1981	29	1	68	2	100	2044	61
Jul-Sep 1982	25	1	72	2	100	1906	53
Jul-Sep 1983	36	*	62	2	100	1868	74
Jul-Sep 1984	40	1	58	1	100	1876	82
Jul-Sep 1985	36	*	62	2	100	1809	74

*Less than 0.5 percent.

The question was: "If there were a major purchase that you wanted to make, do you think now is a time when it would be O.K. to use some of your savings or is now a time when you would be especially reluctant to use some of your savings?"

TABLE C

OPINIONS ABOUT WHETHER NOW IS A GOOD TIME TO USE CREDIT FOR MAJOR PURCHASES

	Use of Credit...						
Survey Date	OK; not reluctant	Pro-con	Not OK; reluctant	Don't know; NA	Total	# cases	Relative score
Jul-Sep 1980	15	1	83	1	100	1793	32
Jul-Sep 1981	13	1	83	3	100	2071	30
Jul-Sep 1982	12	1	85	2	100	2083	27
Jul-Sep 1983	27	1	71	1	100	2057	56
Jul-Sep 1984	27	*	72	1	100	2029	55
Jul-Sep 1985	29	*	70	1	100	1945	59

*Less than 0.5 percent.

The question was: "If there were something that you wanted to buy, do you think that now is a time when it would be O.K. for you to buy it on credit, or is now a time when you would be especially reluctant to take on new debt?"